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Questions
and
Answers
about a
Cooperative

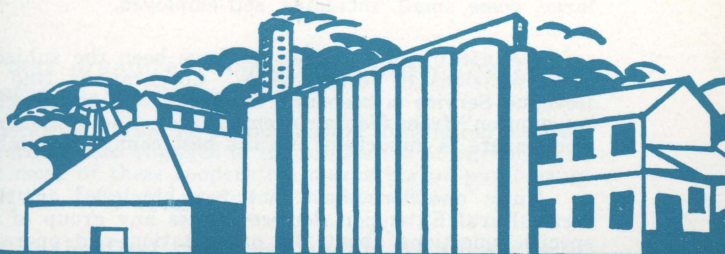
How
to
Make it
Operate
Successfully

How
it Is
Organized

1975
Revision

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Farmers' Cooperative Handbook



TEXAS AGRICULTURAL EXTENSION SERVICE
THE TEXAS A&M UNIVERSITY SYSTEM
John E. Hutchison, Director, College Station, Texas

Preface

This handbook has been prepared to help farmers become better acquainted with the cooperative way of doing business—how a cooperative can be organized and some of the ways to make it work. The question and answer pattern has been followed so as to break down the subject into small parts that can be easily understood.

In 1921 when the Texas Legislature passed the Cooperative Marketing Act it made the following declaration of policy:

“In order to promote, foster and encourage the intelligent and orderly marketing of agricultural products through cooperation and to eliminate speculation and waste; and to make the distribution of agricultural products as direct as can be efficiently done between producer and consumer; and to stabilize the marketing problems of agricultural products; this law is passed.”

Several farmers' cooperatives in the State had been in existence 10 or more years when this law was enacted and have continued in successful operation ever since. Hundreds of other cooperatives have been organized since 1921 and have served their members well.

Many farmers of Texas have had no experience with cooperatives. They are finding their lot as individuals increasingly difficult as they buy and sell in a business world of corporations, chainstores, combines, trusts and unions.

Business groups generally have found the corporation a useful tool for concentrating capital to do jobs too big for the small investor or operator. The nation's 4 million farmers are by far the largest group of small independent businessmen in the country. Business statistics indicate that there are about 2 million commercial businesses, some large, some small, including self-employed.

The affairs of cooperatives have been the subject of a number of court decisions in recent years. Cooperatives find that the Internal Revenue Service is becoming more exacting before granting a letter of “exemption” from federal income taxes. The language used in organization papers is important and the best counsel available should be used.

Many questions have not been included in this bulletin. The Agricultural Extension Service invites any group of farmers to submit specific questions about the organization and operation of their own cooperative.

This bulletin originally was prepared by the late M. C. Jaynes and R. W. Cooper, former specialists in Extension organization and cooperative marketing.

farmers' Cooperative Handbook

JOHNNY FEAGAN

Extension Economist-Organization
The Texas A&M University System

Questions and Answers

Many questions have not been included in this bulletin. The Texas Agricultural Extension Service invites any group of farmers to submit specific questions about the organization and operation of their own cooperative.

1. Q. What is a farmer's cooperative?

A. It is an organization of agricultural producers chartered to transact collectively business pertaining to agricultural products, supplies or services. The Texas Cooperative Marketing Act gives such associations legal status and defines their purpose and powers. (Copies of this Act may be obtained from the State Commissioner of Agriculture, Austin, Texas, or from the Texas Agricultural Extension Service, College Station, Texas.)

2. Q. What are some of the advantages farmers have found from cooperative action?

A. Farmers use cooperatives to process, store and market their produce and to purchase supplies and services. Cooperative processing plants prepare their crops, livestock and livestock products for market. Marketing associations are used to obtain for their members the highest possible price for their products, quality considered. The cooperative purchasing association, on the other hand, assists its members in obtaining their farm supplies at the lowest possible price. Cooperatives have the opportunity of encouraging production of quality agricultural products by returning premium prices to farmers who deliver high-quality products. Through cooperatives, farmers often are able to provide themselves with better service than they were receiving from other agencies. Successful cooperatives save money for their members, giving service at cost. By reducing the cost of getting goods from the producer to the consumer, cooperatives encourage consumption and expand markets. Working together for mutual helpfulness makes a better citizenship.

3. Q. Who may organize a cooperative under the Texas Cooperative Marketing Act?

A. A cooperative marketing or purchasing association may be formed by five or more persons engaged in the production of agricultural products. Three or more of these cooperative marketing or purchasing associations may form a federated cooperative association.

4. Q. What is the first step that should be taken by a group of agricultural producers considering the organization of a cooperative?

A. At a meeting of producers, cooperative marketing or purchasing should be discussed thoroughly as it applies to the commodities

under consideration and to local conditions. The prospective members should determine whether: (1) there is a real need for a producer-owned and controlled association; (2) a cooperative can do the job better than it is now being done; (3) there is sufficient volume of business to assure savings to the members; (4) the members can be depended on for loyal support in bad times as well as good; (5) some outsider is encouraging the formation of the cooperative in order to sell property or equipment or get a job; (6) the producers are willing to put their own capital into a cooperative enterprise; and (7) competent and aggressive leadership is available. The answers to these and similar questions will have a direct bearing on the success or failure of a new association.

5. Q. What is the next step?

A. If the decision is to go ahead, the group then should elect at least five producers as incorporating or temporary directors. These directors may be instructed by the group to complete the organization, obtain a charter, prepare bylaws for the consideration of the new association and to take such other action as may be desirable.

6. Q. How can a charter be obtained?

A. The incorporating directors must prepare articles of incorporation. These articles, after being signed by the incorporating directors and acknowledged before a notary public, are sent to the Secretary of State, Austin, Texas. (Suggested articles of incorporation which should be revised by legal counsel to fit local conditions, may be found in this bulletin.) Issuing and delivering the charter usually requires only a few days if the articles of incorporation of the association are submitted in proper form.

7. Q. Is there any cost to obtaining a charter?

A. A fee of \$10 is required by the Secretary of State for issuing the charter and making the necessary records. This fee should accompany the articles of incorporation when sent to the Secretary of State at Austin.

8. Q. When should the first membership meeting be held?

A. Not later than 30 days after filing the articles of incorporation, the members of the association should hold their first meeting and adopt appropriate bylaws. (Suggested bylaws, which should be adapted to local needs, may be found in this bulletin.) The directors should be elected at this meeting.

9. Q. What records should be kept?

A. Records of the action taken at early meetings of cooperatives sometimes are lost. These may be very valuable later. Minutes of all membership and directors' meetings should be carefully preserved. Accurate records of all funds received and disbursed should be kept from the very beginning so that they will be understandable even years later. Nothing should be left to memory or to loose papers. Bound minute books and ledgers are much safer. The secretary, treasurer,

or the secretary-treasurer is charged with the responsibility of preserving these important records.

10. Q. Who may become members?

A. An association may admit as members all persons engaged in the production of agricultural products. One cooperative, as an organization, may hold membership in another association.

11. Q. What is required of a member?

A. The requirements for membership are determined by the members as set forth in the bylaws. Usually they specify that a member must be a producer of agricultural products and purchase a share of common stock or pay a membership fee. The association may require a member to execute a marketing contract binding the member to handle all or any specified part of certain agricultural products through the association.

12. Q. How much stock may one member own?

A. The Texas laws state: "No stockholder of a cooperative association shall own more than one-twentieth of the issued common stock of the association." This may be further limited in the bylaws. Ownership of preferred, or nonvoting stock, is not limited by law.

13. Q. Do stockholders vote according to the shares of stock owned?

A. No, the Texas law reads: "No member of the association is allowed more than one vote because of the stock or membership capital he may own therein."

14. Q. Must stock purchases or membership fee be paid in cash?

A. A stock or membership certificate may not be issued to a member until it has been fully paid for. Promissory notes of the members may be accepted as full or partial payments. However, associations with small paid-in capital are in poor position either for operating or for obtaining credit.

15. Q. Are members of a cooperative liable for debts incurred by the association?

A. No. Except to the extent of any stock owned in the association or any unpaid balance on a promissory note given in payment for stock or membership fees.

16. Q. How do cooperatives acquire capital to pay for and operate gins, grain elevators, packing plants, etc?

A. If the cooperative is to belong to the members, these members must supply much of the capital used in their business. Some capital usually is raised in cash at the time the cooperative is organized.

In most instances, that is not enough. Additional capital may be acquired by retaining or borrowing a small sum on each unit handled by the cooperative, on each bale of cotton ginned, each pound of butterfat processed, each box of fruit packed, each bushel of grain sold, each dollar's worth of goods supplied, etc. Members contribute this capital in exact proportion to the use they make of the facilities of the association and receive certificates of stock or equity accordingly.

17. Q. What is meant by "revolving capital?"

A. In time, these small amounts invested by the members from each unit of product they deliver to or purchase from their association will pay off indebtedness, pay for physical property and also set up operating capital and reserves. By continuing to retain these small amounts each year, even after the indebtedness is paid, the cooperative can soon pay off the oldest certificates of stock or certificates of equity. In this way the members who actively use the association own and control it. Members who furnish capital in earlier years, but who have moved or for other reasons quit doing business with the association, are gradually paid off as the new capital becomes available. This plan has much to recommend to groups forming new cooperatives or those reorganizing old associations.

18. Q. Where may cooperatives obtain credit?

A. In addition to the usual lending agencies, the Houston Bank for Cooperatives, Houston, Texas, is a possible source of credit for Texas cooperative associations. The bank was established under the Farm Credit Act to furnish credit to farmers' cooperatives. Such loans are made in accordance with good banking practices, with adequate security and an acceptable plan for repayment. A booklet describing cooperative credit and the services available from this bank may be received by writing the Houston Bank for Cooperatives, Houston, Texas.

19. Q. Can a cooperative handle products for persons who are not members?

A. Yes. A cooperative may do business with nonmember producers as long as the nonmember business does not exceed in value the business done with members. However, it is the policy of most cooperatives to keep the amount of nonmember business as low as possible. Regular patrons, if eligible, should become members.

20. Q. On what basis does a cooperative deal with its members?

A. Different plans are followed. It is considered good practice among marketing associations to advance only a reasonable part of the market value at the time products are received from the producer. After the association has performed such marketing services as grading, processing, packing, shipping, selling, etc., the actual cost of these services is deducted, and dividends on capital paid, any sum remaining is returned to the producers as final payment. Many associations retain an amount of money on each unit of produce handled which becomes the member's investment to supply working capital and reserves.

21. Q. How would this plan work in the case of a cooperative cotton gin?

A. Each producer will pay to his cooperative gin at the time of ginning a rate sufficiently high to cover the expense. At the end of the season, after all expenses such as salaries, labor, fuel, repairs, depreciation, insurance and taxes, are paid, the amount of the net saving for the season can be determined. The directors will then provide for the distribution of this net margin or saving. If the association is in debt, a portion of the cash payment to members may be withheld for payment of principal installments and interest. For these amounts withheld, each member will receive stock, certificates of equity or book credit. In this way the capital of the association is built up. From any cash remaining, the directors will provide for payment of limited dividend on the capital invested in the association. They also will set up reserves and the remainder shall be paid to the members as a cash patronage refund based on the amount of business each has done with his association.

22. Q. How would a purchasing association operate under this plan?

A. Supplies are sold to members at cost plus a safe and substantial margin, but usually at prevailing prices. Periodically, savings above operating costs and necessary retains for capital and reserves are returned to members in proportion to their purchases. Price cutting at the time supplies are delivered disturbs business and has led to disastrous price wars. Selling at regular market price enables associations to return larger patronage refunds.

23. Q. What kinds of reserves may directors set up?

A. Directors may set up capital reserves, as reserves for contingencies, and valuation reserves, as reserves for bad debts and depreciation. Capital reserves must be allocated and disclosed to patrons of an association if to be permitted to exclude such reserves from income. Cooperatives are subject to the same rules with respect to setting up valuation reserves as are all other corporations.

24. Q. Do cooperatives extend credit to members?

A. "All business for cash" was one principle of the early cooperatives. Time has proved the soundness of this rule. Cooperatives should treat all members alike and if credit is given one, others will demand it. Few cooperatives can operate on a 100 percent cash basis, yet many are so careful in handling accounts that they have practically no loss. Supply cooperatives have a serious problem, for example, when they deliver fuel oil to the farms or when a hired hand hauls out a load of feed. Cash payments, if required, would work a hardship on the patrons. Directors often instruct the manager to extend credit in such cases, but to require payment for the last purchase before making another credit sale to those particular patrons. In that way, accounts are prevented from getting out of control.

25. Q. Do cooperatives pay dividends on capital stock?

A. Most of them pay reasonable dividends on the capital stock invested by members or others. This rate may not exceed 8 percent per annum under the Texas law. Often the rate is 3, 4 or 5 percent.

This dividend payment must first be earned, then declared by the board of directors. The dividend rate set in the bylaws should be the rate which the association may reasonably expect to pay. There are some disadvantages to authorizing a rate of dividend higher than the one paid, particularly if an association should find itself on a "nonexempt" basis.

26. Q. Do all cooperatives pay cash patronage funds?

A. It is the ultimate aim of cooperatives to return all net margins to patrons. Generally, 20 percent or more of the current patronage refunds are made in cash. In the early life of an association the remainder is retained by the association for paying off loans for capital investments and investment stock is issued to the patron. When funds are available cooperatives revolve out the oldest outstanding stock certificates.

27. Q. Is the practice of leaving margins in a business peculiar to farmers' cooperatives?

A. By no means. Most of the large and successful commercial businesses in the country started with small investments. Year after year, a part of the profits are "plowed back" into the business. Cooperatives, in following this practice, are acting in good American business tradition.

28. Q. Are there benefits other than patronage refunds to be obtained from a cooperative?

A. Yes. Farmers can often improve the quality of service they receive. By mixing their own feed or fertilizer, they can be sure that the formulas used meet their requirements. It is not practical for large manufacturers that distribute over many sections to do this. Keeping ownership and control of marketing, processing and distributive facilities in the hand of a large group of citizens reduces the concentration of economic power.

29. Q. Who determines the business policies of a cooperative?

A. The affairs of the association are managed by the directors, elected by the members from their own number. The board of directors, as a body, establish policy and maintain general control of the business. The manager executes the policies of the board and maintains direct control of the business. Provision is made in the law for referring certain important matters to the membership for its consideration and action. Members may influence the business policies to be followed by attending membership meetings, expressing their views and by helping to elect directors who share their ideas as to how the business should be operated. Since the members own the cooperative, they should feel free to let their wishes be known.

30. Q. What protection have members from dishonest employees?

A. The Texas law requires that all officers or employees handling funds or property be adequately bonded. Directors who fail in

this responsibility may be held personally liable, under the law, for all losses which may occur because of their failure to require proper bonds.

31. Q. What protection have members against inefficient management?

A. Managers of cooperatives are selected by the board of directors. The best interests of the members demand that they elect directors who have courage and sound judgment and who are willing to guard against inefficient management. Active participation of the members in elections and membership meetings is necessary to prevent an unhealthy condition of the cooperative. No relative of a member of the board of directors or of the manager should be employed by the association on a permanent basis.

32. Q. What other qualifications should members expect in directors?

A. Members might well raise the following questions when considering the fitness of a nominee for the important responsibility of director:

Will he give the necessary time and attention to the business of the cooperative? Has he conflicting interests? Has he a near relative engaged in a competing business? Has he shown sound judgment in handling his own business? Will he require a strict accounting for all funds and property handled by employees? Has he the qualities of leadership that will attract members—and beget public confidence? Is he progressive enough to keep the association moving ahead—yet conservative enough to avoid unwise expansion?

33. Q. Do cooperatives pay taxes?

A. Yes. Cooperatives pay the usual state, county, city and school taxes on their properties. They also pay excise, transportation, communication, unemployment taxes, social security, occupational license taxes and a special license fee collected from farmers' cooperatives only. In fact, cooperatives pay taxes of these types on the same basis as do comparable businesses owned by others.

Cooperative associations are not "exempt" from payment of federal corporate income taxes. They may, however, deduct from income those margins which are distributed as patronage refunds if they meet the provisions of Federal law and of regulations of the Internal Revenue Service. (See questions 34, 35 and 36.) The right to deduct from taxable income, amounts distributed on a patronage basis is not limited to a cooperative association. Any business organization or individual may do likewise if the refunds are made pursuant to a pre-existing binding contract between the business and the patron.

A cooperative association which can meet these requirements will not be subject to payment of (1) capital stock issuance and transfer taxes, (2) excess profit taxes, (3) a tax on dividends paid on its capital stock during the fiscal year and (4) a tax on non-patronage income (such as income on business with the United States, rents and interest) paid out on a patronage basis, if distributed within 8½

months after the year in which they were derived. They do, therefore, enjoy a degree of tax exemption.

For want of a better term, the associations which can qualify under Section 521, Title 26, of the Internal Revenue Code of 1954 for a "letter of exemption" generally are referred to as "exempt" cooperatives as distinguished from cooperatives which elect to pay income tax on unallocated margins which are retained as property of the associations.

34. Q. What requirements must an association meet to qualify for a "letter of exemption" under Section 521, Title 26, of the code?

A. Briefly stated, a cooperative must meet the following requirements to qualify for a "letter of exemption."

1. The association must be owned by producers of agriculture commodities. Substantially all voting rights must be owned by actual producers who patronize the association.
2. The association must not do more business with nonmembers than with members.
3. The rate of dividends (or interest) on capital shares must not exceed 8 percent or the legal interest rate of the state, whichever is greater.
4. Operations must be of a mutual nature with nonmembers treated equally with members in business dealing and in the distribution of savings.
5. Patronage records must be maintained and permanently preserved.
6. Purchasing associations must not make purchases for nonmembers who are also nonproducers (not farmers) in excess of 15 percent of the total volume of business.
7. Valuation reserves may be established by cooperative associations in like manner and to the same extent as such reserves may be established by other businesses. Capital reserves, however, must be allocated on a patronage basis to be nontaxable to the cooperative. (See question 23.)
8. The legal structure of the association must be cooperative in principle.
9. Patronage refunds must be allocated and distributed to patrons under a binding obligation to do so.
10. Notice of the allocations and distribution must be given to the patrons in writing.

Many of the difficulties between cooperatives and the Internal Revenue Service come from failure to answer correspondence and make prompt reports. When farmers go into business, they must be businesslike. Officers and employees should be instructed to reply to all important mail.

35. Q. How may a cooperative obtain the "letter of exemption?"

A. While cooperatives meeting these requirements are eligible to exclude their net margins from income and be exempt from the capital stock issuance and transfer tax, excess profits tax and a tax on dividends properly paid on outstanding capital stock, this exemption must in all cases be sought. Application for this exemption is made on Treasury Form No. 1028, a copy of which may be obtained from the Director of Internal Revenue, Dallas, Texas or Austin, Texas. This form is a questionnaire which should be completed and sent to the nearest Director of Internal Revenue. Determination will then be made whether the association may qualify. When an association receives its letter of exemption, its tax return is prepared on Form 990-C instead of the ordinary corporation tax return form.

36. Q. How does the Revenue Act of 1962 affect taxation of farmers' cooperatives?

A. Section 17 adds a new Subchapter T to the Internal Revenue Code of 1954. The new law preserves the principle of a *single, current* tax on income produced through farmer cooperatives, provided they:

1. Adhere to certain requirements as to the *form* in which they distribute patronage refunds.
2. Make distributions within the prescribed time.

The exclusion of margins from taxable income is allowed if such margins are distributed equitably to the patron on a patronage basis pursuant to a pre-existing binding contract, at least 20 percent of the distribution is in cash, property on which a current value can be placed or a qualified check, and if qualified written notice of allocation is made within 8½ months following the close of the cooperative's fiscal year. This exclusion is predicated upon the fact that the margins are not profits belonging to the cooperative as a corporate entity, but represent income to the patron and are taxable to him as such.

37. Q. Does the Revenue Act of 1962 affect farmer cooperatives in any other respect?

A. Yes. Section 19 revises sections 6041, 6042, 6044, 6652 and adds a new section 6049 to the Code. Generally, these changes establish the requirement for corporations to report annually certain dividend, interest and patronage dividend payments. In addition, these payers of interest, dividends or patronage dividends are required to furnish to the recipients of these payments annual statements showing the amounts paid to them as reported on the information returns filed with the Internal Revenue Service. Penalty provisions are provided for failure to file the required information returns.

38. Q. Can patronage refunds to nonmembers be made in the form of book credit toward the purchase of voting stock or acquiring membership?

A. Yes, the Treasury Department has ruled that patronage refunds may be credited to the nonmember until he pays for voting

stock or pays his membership dues, and still meet the requirement that the association deal with members and nonmembers alike.

39. Q. What is the reason for "exempting" cooperatives from the federal income taxes paid by many other corporations?

A. A cooperative acts for and in the interest of its patron. Produce is processed or marketed or supplies are purchased for the member. The association deliberately underpays the farmer for his produce or overcharges him for his supplies and services. The cooperative contracts with its patrons to refund the amounts withheld, after paying the costs of doing business and setting up necessary business reserves. Amounts so withheld by the association are for the account of the patron, held temporarily in the business and eventually returned to the rightful owner as final settlements of business transactions. It is a well-established principle of law that an agent, as such, is not liable for tax on funds he temporarily holds in trust for the principal. It is difficult to see how a nonprofit business could be liable for a tax on profits which it does not make. The difference between the savings dollar of a cooperative and the profit dollar of a commercial business is that the savings dollar goes back to the patron whose business made the saving possible, while the profit dollar of the commercial enterprise very properly goes to those who invested their capital in the business.

40. Q. Is the cooperatives movement antagonistic to democratic government?

A. A cooperative is simply a democratic way of doing business and thrives best in democratic soil. If the aims, objectives and practices of cooperatives were not entirely American and wholesome, over two-thirds of the farmers and ranchmen in Texas would not own and use them.

41. Q. What is the attitude of the Federal Government toward farmers' cooperatives?

A. The Congress has recognized that farmers need a special type of business organization. The Capper-Volstead Act set forth the purposes for which cooperatives may be organized and the powers they may exercise. The Farm Credit Administration, created by Act of Congress, provides credit to meet the various needs of cooperatives. The Farmers Cooperative Service of the United States Department of Agriculture conducts research studies and service activities of assistance to farmer cooperatives. There are many evidences that the Federal Government is sympathetic with farmers in their efforts to help themselves.

The report of the Committee on Small Business of the House of Representatives contains the following paragraph:

"The enactment and reenactment of section 101 (12) and (13) of the Internal Revenue Act appears to represent a continuing attitude on the part of the Congress that the maintenance of a sound agricultural economy is necessary for the preservation of the national well-being. It has now become an established national policy co-existent with all other policies designed to extend all possible support and assistance to

agriculture. This policy apparently is further reflected in state legislation and the combined policy has been affirmed enumerable times by the Supreme Court."

Both the major political parties have repeatedly endorsed the principles of cooperation among farmers and have pledged their support to farmers in their business organizations.

42. Q. Are farmers the only ones who use cooperatives to serve their interests?

A. No. The business world has found cooperative principles useful in many ways. Newspapers have their large news gathering cooperative; retail merchants have their cooperative wholesale establishments; other merchants have their mutual insurance service; banks have their cooperative clearing house arrangements; railroads have cooperative provisions for operating union stations and the interchange of cars. Many examples could be listed.

43. Q. Do many cooperatives fail?

A. Some do, as a matter of course. Some should never have been organized. Others are launched with insufficient educational work among the members. Taken as a group, cooperatives have a much better record of survival than have businesses in general. A survey made by the Farm Credit Administration inquired into the cause of the failure of a number of cooperatives. Briefly summarized, the reasons assigned for cooperative failures were as follows:

- (a) Difficulties in management—high overhead, inadequate accounting, speculation, friction among board members, etc.
- (b) Difficulties in membership—lack of necessary information among members, inexperience of farmers in co-operating, promises of big refunds unfulfilled, etc.
- (c) Financial difficulties—under-financed by members, too liberal credit, over-borrowing, fire loss with insufficient insurance, insistence of members on refunds when cash is needed in business, operating with too small margins, lack of financial reserves, etc.
- (d) Insufficient volume of business—failure to check carefully on volume available before organization, failure of members to patronize the business, over-expansion of facilities, changes in production of crops and livestock, etc.
- (e) Defective legal organization—failure to incorporate, neglect in observing the terms of the charter, bylaws and contracts, etc.

Articles of Incorporation for Capital Stock Cooperatives

Capital stock cooperatives are generally set up on one of two patterns. The cooperative may issue common and preferred stock, or it may choose to issue common, first preferred and preferred stock.

On page 17 in the handbook, Article VIII has been written for the cooperative issuing common, first preferred and preferred stock and should be inserted in the Articles of Incorporation in lieu of Article VIII appearing on page 15.

SPECIMEN FORM FOR ORGANIZATIONS HAVING COMMON AND PREFERRED STOCK

ARTICLES OF INCORPORATION

We, the undersigned, all of whom are residents and citizens of the State of Texas, engaged in the production of agricultural products, do hereby voluntarily associate ourselves together for the purpose of forming a nonprofit cooperative marketing association with capital stock, under the Cooperative Marketing Act of the State of Texas, as amended.

ARTICLE I

Name

The name of this corporation shall be.....

ARTICLE II

Purpose

The purpose of the association shall be to engage in any activity in connection with the marketing or selling of agricultural products produced by and marketed for its members, or with the harvesting, preserving, drying, processing, canning, storing, handling, shipping, or utilization thereof, or the manufacturing or marketing of the byproducts thereof; or in connection with the manufacturing, selling, or supplying to its members of machinery, equipment, or supplies; or in the financing of the above enumerated activities, or any one or more of the activities specified herein. The association, however, may extend any one of the foregoing activities to the products of and supplies for nonmembers to an amount not greater in value than such as are handled by it for its members.

ARTICLE III

Powers

The association shall have all the powers permitted and granted to associations organized under the Cooperative Marketing Act of the State of Texas, as amended, or as the same may be hereafter amended, it being

intended hereby to embrace all of the powers enumerated in Article 5742, Revised Civil Statutes of Texas, 1925, as amended or as the same may be hereafter amended.

ARTICLE IV

Term

The term for which the association is to exist from the date hereof is fifty (50) years.

ARTICLE V

Place of Business

The principal place of business of the association shall be..... in.....County, Texas, but the association may establish other places of business from time to time.

ARTICLE VI

Registered Office and Registered Agent

Pursuant to the provisions of Article 2.05 of the Texas Non-Profit Corporation Act,.....is designated as the registered office of the corporation and.....with street address ofis designated as its registered agent.

ARTICLE VII

Directors

The business of the association shall be under the management, direction, and control of a board of not less than five (5) directors, and the names and post office addresses of those selected for the first year, and who shall serve until their successors are selected at a stockholder's meeting to be held in accordance with the bylaws of the association, are:

<i>Names</i>	<i>Post Office Addresses</i>
.....
.....
.....
.....
.....

ARTICLE VIII

Captital Stock

Section 1. The authorized capital of the association is \$200,000 of which the sum of \$195,000 shall be designated "preferred stock" which shall be divided into 195,000 shares of a par value of \$1 per share, and the sum of \$5,000 shall be designated as "common stock" which shall be divided into 5,000 shares of a par value of \$1 per share, all of which stock shall be issued in the manner provided in the bylaws.

Section 2. All voting rights shall be vested in holders of the common stock, but no common stockholder shall have more than one vote in the affairs of the association regardless of the amount of common stock owned by him.

Section 3. The holders of preferred stock shall have no preference as to dividends, but in the event of liquidation of the corporation, the holders of such stock shall be preferred up to the par value thereof plus any declared dividends then remaining unpaid thereon.

Section 4. Noncumulative dividends of not to exceedpercent (.....%) per annum shall be payable on the outstanding common and preferred stock, as provided in the bylaws.

Section 5. The common and/or preferred stock issued by this corporation may be retired upon call by the board of directors, subject only to the restrictions and provisions of the bylaws.

Section 6. The bylaws shall provide the method whereby a patron or other stockholder of the association shall be entitled to convert into cash his equities and property interests in the corporation, either prior to or after his withdrawal or expulsion from the corporation and may provide that such method shall be the exclusive method whereby such equities and property interest may be so converted.

Section 7. In the event of liquidation of this corporation, the outstanding preferred stock shall first be retired and the holders thereof shall be entitled to payment therefor at par, plus any declared and unpaid dividends thereon before any payments are made to retire the outstanding common stock.

ARTICLE IX

Patronage Refunds

The net margins or earnings effected by the association shall be distributed annually to persons entitled to receive the same as a patronage refund, in the maner provided in the bylaws.

IN TESTIMONY WHEREOF, we hereunto sign our names this

.....day of....., A.D., 19.....

.....
.....
.....

STATE OF TEXAS

COUNTY OF.....

BEFORE ME, the undersigned authority on this day personally appeared....., known to me to be one of the persons whose names are subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

GIVEN UNDER MY HAND AND SEAL OF OFFICE this the

.....day of....., A.D., 19.....

.....
Notary Public in and for

.....County, Texas

ALTERNATE PARAGRAPH TO BE SUBSTITUTED FOR ARTICLE VII IN ARTICLES OF INCORPORATION, AS SHOWN ON PAGE 15 WHERE THE ASSOCIATION DESIRES TO ISSUE COMMON STOCK, FIRST PREFERRED STOCK AND PREFERRED STOCK.

ARTICLE VIII

Capital Stock

Section 1. The authorized capital of this association is \$250,000, of which sum \$50,000 shall be designated "first preferred stock" divided into 50,000 shares of the par value of \$1 per share; \$195,000 of said capital shall be designated "preferred stock" and shall be divided into 195,000 shares of the par value of \$1 per share; and \$5,000 of said capital shall be designated as "common stock" and shall be divided into 5,000 shares of the par value of \$1 per share, all of which stock shall be issued in the manner provided in the bylaws.

Section 2. All voting rights shall be vested in holders of the common stock, but no common stockholder shall have more than one vote in the affairs of the association regardless of the amount of common stock owned by him.

Section 3. Cumulative dividends ofpercent (.....%) per annum shall be payable on the first preferred stock as provided in the bylaws. Noncumulative dividends of not to exceedpercent (.....%) per annum shall be payable on the preferred stock and common stock without preference as provided in the bylaws.

Section 4. Outstanding capital stock of this corporation may be retired upon call of the board of directors in the manner provided in the bylaws, but none of the preferred stock shall be subject to retirement while any of the first preferred stock remains outstanding.

Section 5. The bylaws shall provide the method whereby a patron or other stockholder of the association shall be entitled to convert into cash his equities and property interests in the corporation, either prior to or after his withdrawal or expulsion from the corporation and may provide that such method shall be the exclusive method whereby such equities and property interest may be so converted.

Section 6. In the event of liquidation of this corporation, the holders of the first preferred stock shall be preferred up to the par value thereof plus any declared dividends then remaining unpaid thereon; thereafter the holders of the preferred stock shall be preferred up to par value thereof plus any declared dividends then remaining unpaid thereon, before any distribution is made to the holders of the common stock.

SPECIMEN FORM OF COMMON STOCK CERTIFICATE

COMMON STOCK CERTIFICATE

NUMBER—

—SHARES

.....Farmers Cooperative Association
....., Texas

Capital Stock \$200,000

THIS IS TO CERTIFY THAT.....
is the owner of.....shares of the Common Stock of

.....Farmers Cooperative Association, a corporation,
which stock is transferable on the books of the corporation only on
surrender of this certificate, in accordance with law and the Articles
of Incorporation and bylaws.

This corporation is a cooperative association organized and existing
under and by virtue of the laws of the State of Texas, with capital
stock of \$200,000 divided into 5,000 shares of preferred stock of a par
value of \$1 per share and 195,000 shares of preferred stock of a par
value of \$1 per share. Noncumulative dividends of not to exceed
.....percent (.....%) per annum may be paid on the stock evidenced
by this certificate, in the sole discretion of the board of directors, as
provided in the bylaws and as authorized by law.

The stock evidenced by this certificate may not be transferred to or
owned by any person not engaged in the production of agricultural
products, and no transfer of this certificate in violation hereof or of
the bylaws, shall be valid for any purpose.

The stock evidenced by this certificate may be retired upon call of
the board of directors of the corporation, subject only to the restrictions
and provisions of the bylaws.

All voting rights in this corporation are vested in the holders of
the common stock, but no such holder shall have more than one vote
regardless of the number of shares of common stock owned by him.

In the event of dissolution of the corporation, all outstanding classes
of preferred stock issued by this corporation shall be preferred in the
order of their preference, as to the assets, up to the par value of such
stock plus any dividends declared and unpaid thereon, before any of
such assets shall be distributed in retirement of the common stock.

IN WITNESS WHEREOF, the undersigned corporation has caused
this certificate to be issued by its duly authorized officers this.....day
of.....A.D., 19.....

.....Farmers Cooperative Association
By.....
President

ATTEST:

.....
Secretary

(Seal)

SPECIMEN FORM OF PREFERRED STOCK CERTIFICATE

PREFERRED STOCK CERTIFICATE

NUMBER—

—SHARES

.....Farmers Cooperative Association

....., Texas

Capital Stock \$200,000

THIS IS TO CERTIFY THAT.....

is the owner of.....shares of the preferred stock of

.....Farmers Cooperative Association, a corporation,
which stock is transferable on the books of the corporation only on
surrender of this certificate, in accordance with law and the Articles
of Incorporation, and bylaws.

This corporation is a cooperative association organized and existing
under and by virtue of the laws of the State of Texas, with capital
stock of \$200,000 divided into 5,000 shares of common stock of a par
value of \$1 per share and 195,000 shares of preferred stock of a par
value of \$1 per share. Dividends on the stock evidenced hereby may be
paid in the sole discretion of the board of directors in an amount not
to exceedpercent (.....%) per annum, in accordance with law
and as provided in the bylaws. No voting rights are vested in the
holders of preferred stock of this corporation, all voting rights being
vested in the holders of the common stock.

The stock evidenced by this certificate may be retired upon call of
the board of directors of the corporation, subject only to the restrictions
and provisions of the bylaws.

In the event of dissolution of the corporation, the owners and
holders of preferred stock of the class evidenced by this certificate shall
be preferred over the holders of the common stock in the distribution
of the assets of the corporation up to the par value of such preferred
stock plus any declared and unpaid dividends thereon before any
distribution is made to the holders of the common stock.

IN WITNESS WHEREOF, the undersigned corporation has caused
this certificate to be issued by its duly authorized officers this.....day
of.....A.D., 19.....

.....Farmers Cooperative Association

By.....
President

ATTEST:

.....
Secretary

(Seal)

SPECIMEN FORM OF FIRST PREFERRED STOCK CERTIFICATE

FIRST PREFERRED STOCK

NUMBER—

—SHARES

.....Farmers Cooperative Association

....., Texas

Capital Stock \$250,000

THIS IS TO CERTIFY THAT.....

is the owner of.....shares of the first preferred stock of

..... Farmers Cooperative Association, a corporation which stock is transferable on the books of the corporation only on surrender of this certificate, in accordance with law and the Articles of Incorporation, and bylaws.

This corporation is a cooperative association organized and existing under and by virtue of the laws of the State of Texas, with capital stock of \$250,000 divided into 50,000 shares of first preferred stock of a par value of \$1 per share; 195,000 shares of preferred stock of a par value of \$1 per share; and 5,000 shares of common stock of a par value of \$1 per share. Cumulative dividends ofpercent (.....%) per annum shall be paid on the stock evidenced by this certificate, as provided in the bylaws and as authorized by law. No voting rights are vested in the holders of first preferred stock of this corporation, all voting rights being vested in the holders of the common stock.

The stock evidenced by this certificate may be retired upon call of the board of directors of the corporation, subject only to the restrictions and provisions of the bylaws.

In the event of dissolution of the corporation, the holders of the first preferred stock shall be preferred up to the par value of such stock, plus any dividends declared and unpaid thereon, before any of the assets of the corporation may be distributed to the holders of the common or preferred stock of the corporation.

IN WITNESS WHEREOF, the undersigned corporation has caused this certificate to be issued by its duly authorized officers this.....day of.....A.D., 19.....

.....Farmers Cooperative Association

By.....
President

ATTEST:

.....
Secretary

(Seal)

Bylaws for Capital Stock Cooperatives

Capital stock cooperatives are generally set up on one of two patterns. The cooperative may issue common and preferred stock, or it may choose to issue common, first preferred and preferred stock.

On pages 30 and 31 certain sections of Article VI have been written for the cooperative issuing common, first preferred and preferred stock and should be inserted in the Bylaws in lieu of those sections of Article VI appearing on pages 25 and 26.

FORM OF BYLAWS WHICH MAY BE ADAPTED FOR COOPERATIVES HAVING COMMON AND PREFERRED STOCK

ARTICLE I

Purposes

The purposes for which this association is incorporated are those set forth in the Articles of Incorporation.

ARTICLE II

Place of Business

The place where the principal business of the association will be transacted is.....,
County, Texas.

ARTICLE III

Board of Directors

Section 1. Number and Qualifications of Directors. The corporate power, business and property of the association shall be conducted, controlled and managed to the extent authorized by law and by the Articles of Incorporation and these bylaws by a board of..... directors, each of whom shall be a member of this association or an authorized representative of an incorporated member.

Section 2. Election of Directors. At the first annual meeting of the members of this association, directors shall be elected to succeed the incorporating directors. At such meeting directors shall be elected for one (1) year, directors for two (2) years and directors for three (3) years. Thereafter each director shall be elected for a term of three (3) years. At least two members shall be nominated for each directorship. All directors shall be elected by secret ballot, and the nominee receiving the greatest number of votes for each position shall be elected. Directors shall hold office until their successors have been duly elected and qualified.

Section 3. Vacancies. Whenever a vacancy occurs in the board of directors, other than from the expiration of a term of office, the remaining directors shall appoint a member of the association to fill the vacancy until the next regular meeting of the members.

Section 4. Board Meetings. The board of directors shall meet at least once each month in the principal office of the association at a time to be set by the board of directors.

Section 5. Special Board Meetings. Special meetings of the board shall be held upon the call of the president or upon the written request of at least three members of the board. Such written requests shall be signed by the members making the same, shall state the purpose of such meeting, the time and place where it is to be held and shall be addressed and delivered to the secretary of the association. Written notice of all special meetings shall be given to all members of the board at least two (2) days prior to the date of such meeting, provided, however, that such written notice of any meeting may be waived by the directors, by unanimous consent.

Section 6. Quorum. A majority of the members of the board of directors shall constitute a quorum at any meeting of the board.

Section 7. Depository. The board of directors shall have the power from time to time to select one or more banks to act as depositories of the funds of the association, to determine the manner of receiving, depositing, and disbursing the funds of the association, the form of checks to be used and the person or persons who shall be authorized to sign such checks.

Section 8. Employees. The board of directors shall have power to employ or to authorize the employment of a manager and such other employees as may be deemed necessary, to prescribe the duties thereof and to fix their compensation. No director or member of a director's immediate family shall serve on a permanent basis as a manager or employee of the association. No member of the manager's family shall be employed by the association without the unanimous consent of the board of directors.

Section 9. Bonds. The board of directors shall require all officers, employees and agents of the association handling funds or property belonging to, or in the possession or under the control of the association, to furnish the association with a satisfactory bond of indemnity, indemnifying the association and its members against any fraudulent, dishonest or unlawful act on the part of such officers and employees. Such bonds shall be furnished by a responsible bonding company and shall be approved by the board of directors.

Section 10. Executive Committee. The board of directors shall be empowered to appoint from its own membership an executive committee of three members, determine its tenure of office and prescribe the powers and duties of such committee. The executive committee shall keep accurate minutes of its proceedings and shall submit a written report thereof to all directors within seven (7) days following each meeting of the executive committee. Such minutes shall be considered and approved by the board of directors at the next succeeding meeting of the board.

Section 11. Removal. Any member may bring charges against an officer, director or member of the association by filing the same in writing with the secretary of the association together with a petition signed by at least ten (10%) percent of the members of the association, requesting the removal of the officer, director or member in question. The secretary of the association shall give such officer, director or member written notice of the charges, at least ten (10) days prior to the date of the meeting at which the charges will be considered and voted upon. At the next regular or special meeting of the association

a hearing shall be held and such charges shall be considered. The person charged and the person or persons bringing the charges against him shall be given an opportunity to be heard in person or through counsel and to present witnesses. At the conclusion of such a hearing a majority vote of the members shall decide the issue.

ARTICLE IV

Officers

Section 1. Manner of Election. The board of directors shall elect from their number a president and a vice president. They shall also elect a secretary and a treasurer, who need not be directors. The offices of secretary and treasurer may be combined by the board of directors, and the combined office shall be designated as "secretary-treasurer."

Section 2. Tenure of Office. The officers shall hold office at the discretion of the board of directors, subject to the power of removal by stockholders as provided in these bylaws and as authorized and allowed by law.

Section 3. Duties.

(a) *The president shall:*

- (1) Preside over all meetings of the association and of the board of directors.
- (2) Call special meetings of the board of directors and of the stockholders.
- (3) Perform all acts and duties usually performed by an executive officer of a corporation.
- (4) Serve as an ex-officio member of all committees of the association.
- (5) Sign all stock certificates and such other papers and documents as he may be authorized or directed to sign by the board of directors.

(b) *The vice president* shall perform the duties of the president at such time or times as the president shall be absent or disabled. In case of the death, resignation or total disability of the president to perform the duties of his office, the board of directors may declare the office vacant and elect his successor.

(c) *The secretary* shall keep a complete record of all meetings of the stockholders of the association and of all meetings of the board of directors. He shall have general charge and supervision of the books and records of the association. He shall attest or sign as secretary all stock certificates and such other papers pertaining to the association as he may be authorized or directed to do by the board of directors. The secretary shall serve all notices required by law and by these bylaws and shall make a full report to the stockholders at their annual meetings of all matters and business pertaining to the association. He shall keep a proper stock record showing the name and address of each stockholder of the association, the number of his stock certificate(s) and the date of issuance, surrender, cancellation or forfeiture thereof. He shall make all reports required by law and shall perform such other duties as may be required of him by the association or the board of directors. He shall keep in the office of the association all books and

records of the association, and shall maintain a separate permanent file containing copies of the audit reports, letter of exemption, charter, bylaws and amendments thereto. Upon the election of his successor, the secretary shall deliver to him all books and other property in his possession belonging to the association.

(d) *The treasurer* shall keep a complete record of all financial transactions of the association and perform such other duties and exercise such other powers as the board of directors may authorize or direct.

ARTICLE V

Members

Section 1. Qualification of Membership. Any person, firm, partnership, corporation, or association, including landlords and tenants, who is a bona fide producer of agricultural products or any producer of agricultural products who is a purchaser of supplies and/or services provided by this association, may become a member of this association if found acceptable by the board of directors, by purchasing one share of common stock, signing such marketing and purchasing agreements as the board may prescribe from time to time, and by agreeing to comply with the requirements of the Articles of Incorporation and this code of bylaws.

Section 2. Termination of Membership. In the event of the death of a member, or, if the board of directors shall find, following a hearing, that a member has ceased to be a producer of agricultural products or a patron of the association, or has moved out of the territory in which the association is operating, the board of directors may suspend or terminate his membership without prejudice to any of his property rights or equities in the association, and give notice of such action to such member, his heirs or legal representatives, and call for the surrender of his common stock. When such membership is terminated, the board shall call and cancel such common stock in the association owned by such former member, and, in its discretion, pay therefor the par value of such stock in cash, and/or in preferred stock of the association.

Section 3. Annual Membership Review. The board of directors shall review annually its official membership record, and shall determine the membership eligibility status of all persons holding common stock of the association. Such stockholders who are found to be ineligible for membership in the association as provided for in these bylaws shall be notified thereof and given an opportunity to show cause why their common stock should not be called in by the association.

Section 4. Nonmember Business. The association, if it elects to do business with nonmembers, shall deal with nonmember patrons in all respects on the same basis as with members, but the association may not do over fifty (50%) percent of its marketing business with or for nonmember producers. The amount of business in farm business services or in the furnishing of supplies and equipment, which it may do with or for patrons who are neither members nor producers, may not exceed fifteen (15%) percent of all such business.

Section 5. Member Consent. Each person who hereafter applies for and is accepted to membership in this cooperative and each member of this cooperative on the effective date of this bylaw who continues as a member after such date shall, by such act alone, consent that the amount of any distributions with respect to his patronage which are

made in written notices of allocation (as defined in 26 U.S.C. 1388) and which are received by him from the cooperative, will be taken into account by him at their stated dollar amounts in the manner provided in 26 U.S.C. 1385 (a) in the taxable year in which such written notices of allocation are received by him.

ARTICLE VI

Capital Structure

Section 1. Capital Stock. The authorized capital of the association shall be in the amounts and classes of stock as set forth in the association's charter and any amendments thereto. Each share of such stock shall be issued and held subject to the terms, conditions and limitations of the Cooperative Marketing Act of Texas, as amended, the charter of the association, these bylaws and any amendments hereafter made thereto.

Section 2. Transfer of Stock. No stock of this association shall be transferred except on the books of the association, and in no event shall common stock be transferred to or owned by any person not engaged in the production of agricultural products except a bona fide Farmers' Cooperative Association. These restrictions shall be printed on every stock certificate subject thereto.

Section 3. Voting Rights. All voting rights shall be vested in the holders of common stock. No common stockholders shall have more than one vote in the affairs of the association or in the election of its directors, regardless of the amount of common stock owned by him.

Section 4. Stock Subscriptions. The association shall not issue any class of stock to any person until the same shall be paid for in full, in cash or credits on the books of the association.

Section 5. Dividends. Noncumulative dividends of not to exceed percent (.....%) per annum are to be paid on the outstanding stock of the association, if, as and when declared by the board of directors. Such dividends may be paid in cash and/or preferred stock of the association in the discretion of the board of directors.

Section 6. Retirement of Common Stock. In the event of the death or expulsion or termination of the membership of a member, the board shall call and cancel all common stock in the association owned by such former member, and pay therefor the par value of such stock in cash, and/or in preferred stock of the association in its discretion.

Section 7. Retirement of Preferred Stock. The board of directors is authorized at any time and in its sole discretion to call for the retirement at par of the oldest outstanding shares of preferred stock theretofore issued by the association, as determined from the date of original issue. Payment at par shall be made for called shares immediately on delivery and failure of the owners or holders to deliver certificates called for shall entitle the association as the owner's agent or otherwise, to cancel the shares called for retirement at the expiration of thirty (30) days after the call has been made. In the event of such cancellation and failure of the stockholder to surrender the call certificate(s), the proceeds of such cancelled stock shall be placed to the credit of such stockholder and shall be held by the association for the owners' account in accordance with the laws of the State of Texas. The method herein provided for the revolving of capital shall constitute the sole and exclusive method whereby a patron or other stockholder

of the association shall be entitled to convert into cash his equities (property interests) in the association, either prior to or after his withdrawal or expulsion from the association, and shall be in lieu of any right or power any such patron or stockholder might have or be entitled to assert to have his equities appraised by the board of directors or otherwise and be paid therefor on the basis of such appraisal within any given period of time.

Section 8. Stock Retirement in the Event of Death. Notwithstanding the provisions of Section 7 of this article, in the event of the death of a member of the association, the board of directors may, at its discretion, retire common and/or preferred stock owned by such deceased member, having an aggregate par value of not to exceed one hundred dollars (\$100), and pay the par value thereof, plus any declared and unpaid dividends thereon in cash to the heirs or legal representatives of the deceased, upon surrender of the stock certificate or certificates so cancelled and retired and upon the submission of satisfactory evidence that such heirs or legal representatives are the sole persons entitled to receive the funds. Such stocks, up to the amounts specified, may be so called, cancelled and retired, regardless of the date of issue thereof.

Section 9. Liquidation. Neither common nor preferred stock shall have a preference over the other as to dividends, but in the event of liquidation of the association, the outstanding preferred stock shall be first retired and the holders thereof shall be entitled to payment therefor at par plus any declared and unpaid dividends thereon, before any payments are made to retire the outstanding common stock.

ARTICLE VII

Meetings of Stockholders

Section 1. Annual Meeting. The regular annual meeting of the member common stockholders of the association shall be held at the principal place of business of the association, or at such other place within the territory served by the association as may be designated by the board of directors. Such meeting shall be held within sixty (60) days after the close of the fiscal year of the association, at a time and date specified by the board of directors.

Section 2. Special Meetings. Special meetings of the members may be called by the president or by a majority of the board of directors. Each such call shall be in writing and shall state the time, place, and purpose of such meeting. No business shall be transacted at any special meeting other than that stated in the purpose of the call.

Section 3. Notice of Meeting. The secretary shall cause a notice of each special meeting to be mailed to each common stockholder of the association according to his address as it appears on the association's books, at least ten (10) days prior to the date of such meeting. The notice shall state the time, place and purpose of which the meeting was called.

Notice of regular annual meetings shall be given likewise by the secretary, stating the time and place of the meeting.

Section 4. Quorum. Twenty-five percent (25%) of the common stockholders shall constitute a quorum for the transaction of business at any meeting. If on first call twenty-five percent (25%) of common

stockholders fail to attend, then a second meeting shall be called at which the common stockholders present shall constitute a quorum.

Section 5. Voting. No votes by proxy or power of attorney shall be permitted. All ballots in connection with the election of directors shall be cast by members in person in attendance at the stockholders' meeting at which such election is being held. It shall be permissible, however, in connection with any other matter of business of the association, except the election of directors, for the board of directors to cause to be prepared ballots in writing to be cast by the members and transmit such ballots to the members by mail for their further handling. Ballots so transmitted shall contain a clear and concise statement of each issue to be voted upon and shall provide a place where the member may indicate his vote in favor of or against each such issue. Such ballots must be signed by the member casting the ballot and may be transmitted by him through the United States mail to the secretary of the association, or delivered to such secretary in person, to be by him placed in the ballot box in the office of the association prior to the date of the regular or special stockholders' meeting at which such issues are to be voted upon. The envelopes containing the ballots so cast shall not be opened until the vote is counted, at which time such envelopes containing such ballots shall be opened by the counters appointed by the chairman of the meeting. No ballot shall be counted if the envelope containing the same has been opened prior to the time such envelope is delivered to the counters. All eligible ballots cast in the manner aforesaid shall constitute the appearance of the members casting such ballots at the meeting, in determining whether a quorum is present.

ARTICLE VIII

Reserves and Patronage Refunds

Section 1. Margins. It is the ultimate aim of this association to render services to its patrons at cost. In order to operate on a nonprofit and cooperative basis and at the same time to insure the solvency and financial stability of the association, adequate margins shall be withheld by the association on all transactions. Such margins shall at all times be subject to allocation to the patrons entitled thereto in the manner provided by law and in accordance with these bylaws, and shall be so allocated within such period of time as may be prescribed from time to time in the Internal Revenue Code and Regulations thereunder.

Section 2. Reserves. From the margins retained by the association, the board of directors in its discretion, may create and authorize the establishment of reasonable reserves for necessary purpose. All capital reserves so established shall be allocated on the books of the association to the accounts of the various patrons on the basis of the amounts contributed by them to such reserves, and each patron to whom such allocation is made shall be given notice thereof. While the valuation reserves which are established need not be allocated, the records and accounts of the association shall be so kept as to afford a means of making accurate allocations of such reserves on the basis of the contributions thereto, if such reserves are not needed for the purpose for which they were created.

Section 3. Allocation of Reserves. Amounts of savings or margins retained by the association in capital reserves and allocated to the individual patrons, shall have the same status as though they had been

paid to the patrons in cash pursuant to a legal obligation to do so and the patrons had then furnished corresponding amounts of money to the association to be placed in such reserve. The association shall be obligated to repay such capital advances to the patrons making the same, pursuant to the terms and conditions of these bylaws.

Section 4. Annual Study of Reserve Accounts. The board of directors shall make a study of all reserve accounts following each annual audit and shall determine whether any of such reserves shall be retained, increased, reduced and/or revolved. Following such study the board shall direct the disposition to be made of such reserves, make a record of that action in the minutes of such board meetings, and shall issue proper and necessary instruction pursuant thereto.

Section 5. Revolving Reserve Accounts. Whenever it shall appear to the board of directors that an established reserve is adequate for its designated purpose, the board may direct that said reserve be revolved in whole or in part by taking out of such reserve whatever amount the board may direct and pay the same to the patrons according to their allocated equities in the reserve. Such equities shall be revolved out of such reserve in the date order in which they were allocated. The amounts so revolved out of such reserve account shall be replenished from margins retained during the current year's operations, which amounts so retained shall be allocated on the basis of the contributions of the patrons to such reserve.

Section 6. Reducing Established Reserves. Whenever in the discretion of the board of directors conditions justify reducing an established reserve in whole or in part, the board shall order such reduction and direct that the amount of such reduction be distributed to patrons according to their equities therein in the date order in which such equities were allocated.

Section 7. Patronage Refunds. The annual net savings or margins resulting from the transaction of the business of the association in excess of the valuation reserve fund requirements as provided above, and after the payment of dividends on the capital stock outstanding, shall be apportioned to and distributed among the patrons as a cooperative refund for the year, on a patronage basis, as shown upon the books and accounts of the association. Accurate patronage records shall be maintained on a departmental basis to comply with this requirement. Said cooperative refund shall be paid or credited to the account of the patron entitled thereto at least once each year.

At the discretion of the board of directors, funds revolved out of reserves and/or the patronage refunds provided in the preceding paragraph shall be paid to the patrons entitled thereto, in whole or in part, in cash, in certificates of preferred stock, or in book credits; provided however, that in the distribution of such patronage refunds, not less than 20 percent shall be paid in cash—the remainder in qualified written notices of allocation, all patrons shall be treated alike, and there shall be no discrimination between member and nonmember patrons. Following the end of each fiscal year, the association shall notify each patron and stockholder of the association of all amounts allocated to him as a result of the operations of the association during such year, and of all amounts paid or to be paid to him as a dividend on his capital stock for such year. In the event of the payment or allocation of patronage refunds during such year of amounts earned in previous years but not theretofore allocated, the patron shall be given notice thereof.

Section 8. Refunds to Nonmembers. In order to provide a mutuality of risk, as well as benefit, the board of directors shall cause to be deducted from patronage refunds due nonmember patrons who are eligible for membership in the association, an amount equivalent to one share of common stock in the association. Such patron, if approved by the board of directors, shall become a member and a share of common stock shall be issued to him.

Section 9. Undeliverable Refunds. In the event that the association is unable to make payment to any patron of patronage refunds or other sums due such patron because of inability to locate the patron or incapacity of the patron to receive the same, or other cause beyond the control of the association, such unpaid amounts shall be placed to the credit of such patron and held by the association subject to the owner's order, in accordance with the laws of the State of Texas.

Section 10. Losses. In the event the association shall suffer a net loss in its overall operations in any fiscal year, the board of directors shall have the authority to prescribe the manner in which such loss shall be handled.

ARTICLE IX

Miscellaneous

Section 1. Cooperative Association. This corporation shall be operated in all respects within the limitations of the Texas Cooperative Marketing Act as amended or as hereafter amended, for the mutual benefit of its members as producers of agricultural products. The value of business conducted with members shall always be in excess of that conducted with nonmembers, and each member shall be limited to one vote.

Section 2. Reports and Audits. It shall be the duty of the treasurer and the manager to furnish the board of directors at least once each month during the operating season with a statement of assets and liabilities as of the end of the preceding month, and with a statement of income and expense covering the period from the end of the last fiscal year to the end of the preceding month. Immediately after the end of each fiscal year the board of directors shall employ a practicing public accountant who shall make a complete audit of the association's records and furnish the board of directors with a report thereof.

Section 3. Contract with Patrons. The patrons of the association, by dealing with the association, acknowledge that the terms and provisions of the articles of incorporation and this code of bylaws shall constitute a contract between the association and the patron, and both the association and the patrons are bound by said contract, as fully as though each patron had individually signed a separate instrument containing said terms and conditions. Pursuant to such contract, each patron of the association acknowledges constructive receipt of all sums of money which may be allocated to such patron in accordance with these bylaws, as having been delivered to such patron and by him re-invested in capital or capital reserves of the association.

ARTICLE X

Corporate Seal

Section 1. The corporate seal of this association shall consist of two concentric circles surrounding a star. The name of the association shall be included therein.

ARTICLE XI

Amendments

These bylaws may be altered or amended at any regular or special meeting of the members by the affirmative vote of a majority of the holders of the common stock present and voting. No amendment to the bylaws shall be passed, however, unless notice in writing to the effect that the same will be voted upon has been mailed to the address of each holder of common stock of the association.

I HEREBY CERTIFY, that the above bylaws were adopted by the stockholders of this corporation on this.....day of....., A.D., 19.....
.....Farmers Cooperative Association
By.....
Secretary

WHERE AN ASSOCIATION'S CHARTER AUTHORIZES THE ISSUANCE OF "FIRST PREFERRED STOCK" THE FOLLOWING ALTERNATIVE PARAGRAPHS SHOULD BE SUBSTITUTED FOR THE COMPARABLE PARAGRAPHS IN ARTICLE VI IN THE SPECIMEN FORM OF BYLAWS APPEARING ON PAGES 25 AND 26.

ARTICLE VI

Capital Structure

Section 1. (No change)

Section 2. (No change)

Section 3. (No change)

Section 4. (No change)

Section 5. Dividends. Cumulative dividends ofpercent (.....%) per annum shall be paid on the outstanding first preferred stock. Non-cumulative dividends of not to exceedpercent (.....%) per annum may be paid on the outstanding common and preferred stock if, as, and when declared by the board of directors. Such dividends may be paid in cash and/or preferred stock of the association in the discretion of the board of directors.

Section 6. (No change)

Section 7. (No change)

Section 7a. Retirement of First Preferred Stock. The board of directors is authorized at any time, and in its sole discretion to call for the retirement at par of the oldest outstanding shares of first preferred stock theretofore issued by the association, as determined from the date of original issue.

Section 7b. Retirement of Preferred Stock. After all of the outstanding first preferred stock of the association has been retired, the board of directors is authorized at any time, and in its sole discretion to call for the retirement at par of the oldest outstanding shares of preferred stock theretofore issued by the association, as determined from the date of original issue.

Section 7c. Payment at par (plus dividends declared but unpaid thereon) shall be made for all shares of stock called for retirement, immediately upon delivery of the certificate(s) evidencing such shares. Failure of the owners or holders to deliver certificates representing stock called for retirement shall entitle the association as the owner's agent or otherwise to cancel the shares so called for retirement at the expiration of thirty (30) days after the call has been made. In the event of such cancellation and failure of the stockholder to surrender the called certificate(s), the proceeds of such cancelled stock shall be placed to the credit of such stockholder and shall be held by the association for the owner's account in accordance with the laws of the State of Texas.

Section 7d. The method herein provided for the revolving of capital shall constitute the sole and exclusive method whereby a patron or other stockholder of the association shall be entitled to convert into cash his equities (property interests) in the association, either prior to or after his withdrawal or expulsion from the association, and shall be in lieu of any right or power any such patron or stockholder might have or be entitled to assert to have his equities appraised by the board of directors or other wise and be paid thereon on the basis of such appraisal within any given period of time.

Section 8. Stock Retirement in the Event of Death. Notwithstanding the provisions of Section 7a through 7d of this Article, in the event of the death of a member of the association, the board of directors may, in its discretion, retire capital stock of any class owned by such deceased member, having an aggregate par value of not to exceed \$100, and pay the par value thereof, plus any declared and unpaid dividends thereon, in cash to the heirs or legal representatives of the deceased, upon surrender of the stock certificate or certificates so cancelled and retired and upon the submission of satisfactory evidence that such heirs or legal representatives are the sole persons entitled to receive the funds. Such stocks, up to the amount specified, may be so called, cancelled and retired regardless of the date of issue thereof.

Section 9. Liquidation. In the event of liquidation of the association, the outstanding first preferred stock shall first be retired and the holders thereof shall be entitled to payment therefor at par plus any declared and unpaid dividends thereon, before any payments are made to retire the outstanding common and preferred stock. When all of the first preferred stock has been so retired, the outstanding preferred stock shall be first retired and the holders thereof shall be entitled to payment therefor at par, plus any declared and unpaid dividends thereon, before any payments are made to retire the outstanding common stock.



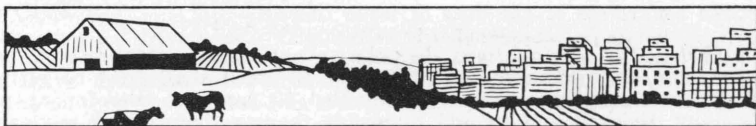
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